Second Quarter 2026 — Economic and Capital Markets Commentary

Wall of Worry

"More money is lost anticipating the changes in the overall stock market than any other way of investing."

– Peter Lynch, Legendary Investor

Equity markets entered 2026 on a strong footing, supported by resilient economic activity and stable inflation prints.

However, as the first quarter progressed, U.S. large-cap stocks faltered a bit, with the tech-focused mega-cap companies known as the "Magnificent Seven" turning broadly negative. This represented a significant rotation away from the pattern of the last few years, during which these mega-caps accounted for an enormous share of market returns. In 2026, the outperformance of large technology companies gave way to the outperformance of those in the energy, industrial, and materials sectors. This rotation was also seen in small and mid-sized companies and in non-U.S. stocks, which outperformed their larger and domestic peers.

Those shifts in the first quarter occurred partially in response to several significant risk factors that reared their heads in 2026. Specifically, the airstrikes in Iran with their impact on petroleum prices and the AI-induced sell-off of software companies' stocks (and more importantly in their bonds), a sign of potential trouble in the world of private credit.

These two risk scenarios are part of the "wall of worry" that the current bull market will have to overcome if it's to sustain itself. However, in the rear-view mirror many years from now, we may view these as just another bump in the road of long-term market returns.

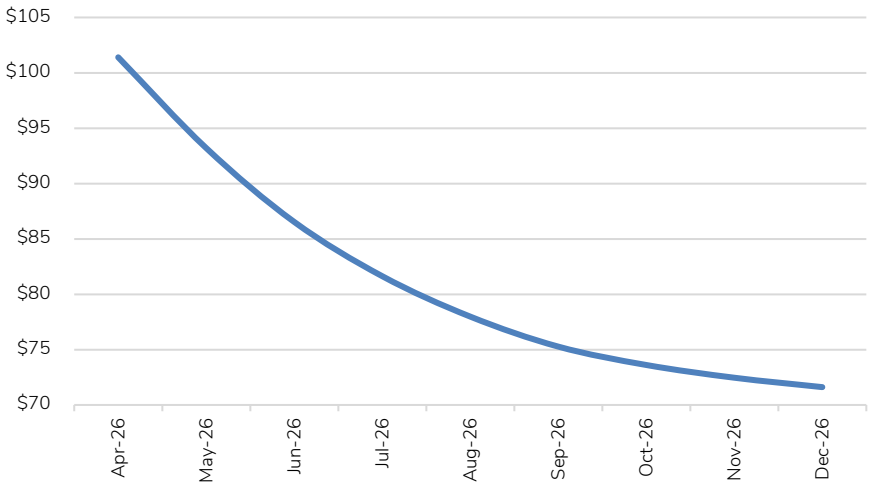
Risk #1: Oil / Gas Prices (here we go again...)

For the second time in the last five years, oil and gas markets convulsed as supply chains were upended, this time by the conflict in the Middle East. In 2022, Russia's invasion of Ukraine shocked markets. However, oil-rich nations were able to increase supply, and oil prices returned to pre-war levels within 6 months.

Today, Iran's semi-closure of the Strait of Hormuz — through which roughly 20 million barrels of oil and oil products flowed each day in 2025, alongside approximately one-fifth of global liquefied natural gas (LNG) trade — has created a supply shock with no modern precedent. Energy experts assume prices will remain high for the duration of the conflict. Notably, however, long-term oil futures contracts for year-end are currently trading under $75 a barrel, reflecting an expectation that the price of oil will be much lower by the end of the year.

Energy price shocks of this magnitude transmit to public equity markets through several channels simultaneously. Most directly, they act as a consumer tax: every dollar increase in the price of a barrel of oil reduces real purchasing power for households and depresses discretionary spending. Continued pressure at the pump risks denting consumer confidence — particularly consequential given that consumer spending represents approximately 70% of U.S. GDP.

US Oil Futures Price (WTI- Month of Expiration)



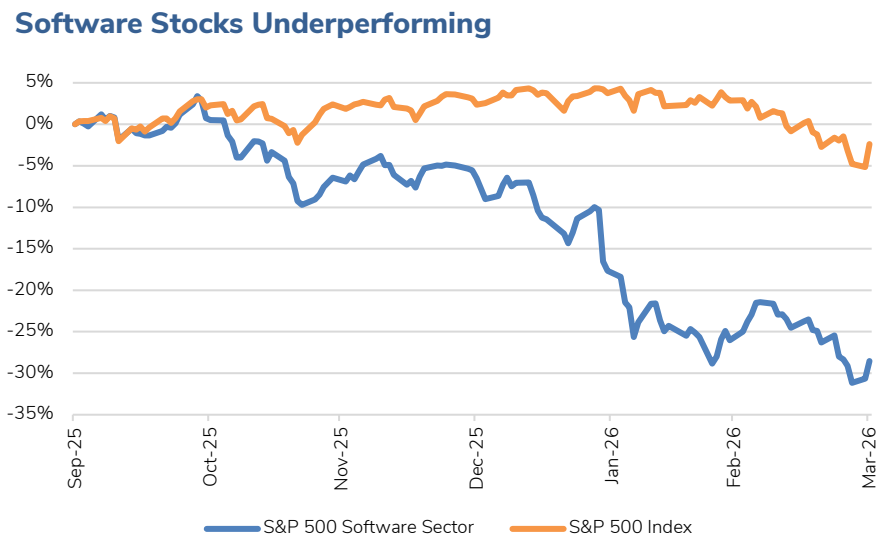
Source: Bloomberg Finance, L.P.

For corporate earnings, the impact is asymmetric. Energy companies, particularly domestic producers insulated from Strait-related disruptions, stand to benefit meaningfully, as higher prices typically incentivize incremental profitable drilling activity. In contrast, energy-intensive industries — airlines, chemicals, shipping, and manufacturing — face margin compression as input costs rise. In any event, the longer the current crisis persists, the more damaging the impact it will have on the global economy.

Risk #2: Private Credit Contagion

As we mentioned in our first quarter commentary, the private credit market has grown substantially since the Great Recession, expanding from a niche institutional strategy to a roughly $3 trillion global market. This market encompasses direct lending, business development companies (BDCs), and the flourishing category of semi-liquid "evergreen" funds. Much of this growth has occurred without a true credit cycle stress test, a downturn in which we learn whether much of this private debt will ever be repaid. That test may now be underway.

The AI productivity we also mentioned in our first quarter commentary has moved into software coding efficiency. One result is the concern that many companies, who normally purchase software from outside vendors, will now utilize AI to build their own software applications. This could cripple the revenue generation of these software companies and threaten their ability to meet their previously mentioned debt obligations.



Source: Bloomberg Finance, L.P.

This is particularly worrisome because software is arguably the largest sector in the entire private credit market, making up anywhere from 25-35% of outstanding loans, depending on the classification. Many of these companies had high-margin, recurring revenue, so the loans were considered relatively safe, despite being asset-light companies. That revenue may now be in jeopardy.

Potential AI disruption of the sector has spooked credit investors, who demanded withdrawals from many funds during the first quarter. Immediate liquidity demands from illiquid assets are

never a good combination, and many private credit funds had an uncomfortable choice between selling illiquid assets at distressed prices or limiting fund redemptions (which many did).

All of this has the potential to begin a downturn in the classic credit cycle, resulting in a prolonged "slow bleed" — a gradual credit contraction that suppresses business investment and economic growth over an extended period rather than producing a sudden market dislocation. While a crisis in private credit might not impact financial markets as severely as mortgage-backed securities and collateralized debt obligations did in 2008, rising defaults in private credit have the potential to ripple through the financial system in a negative way.

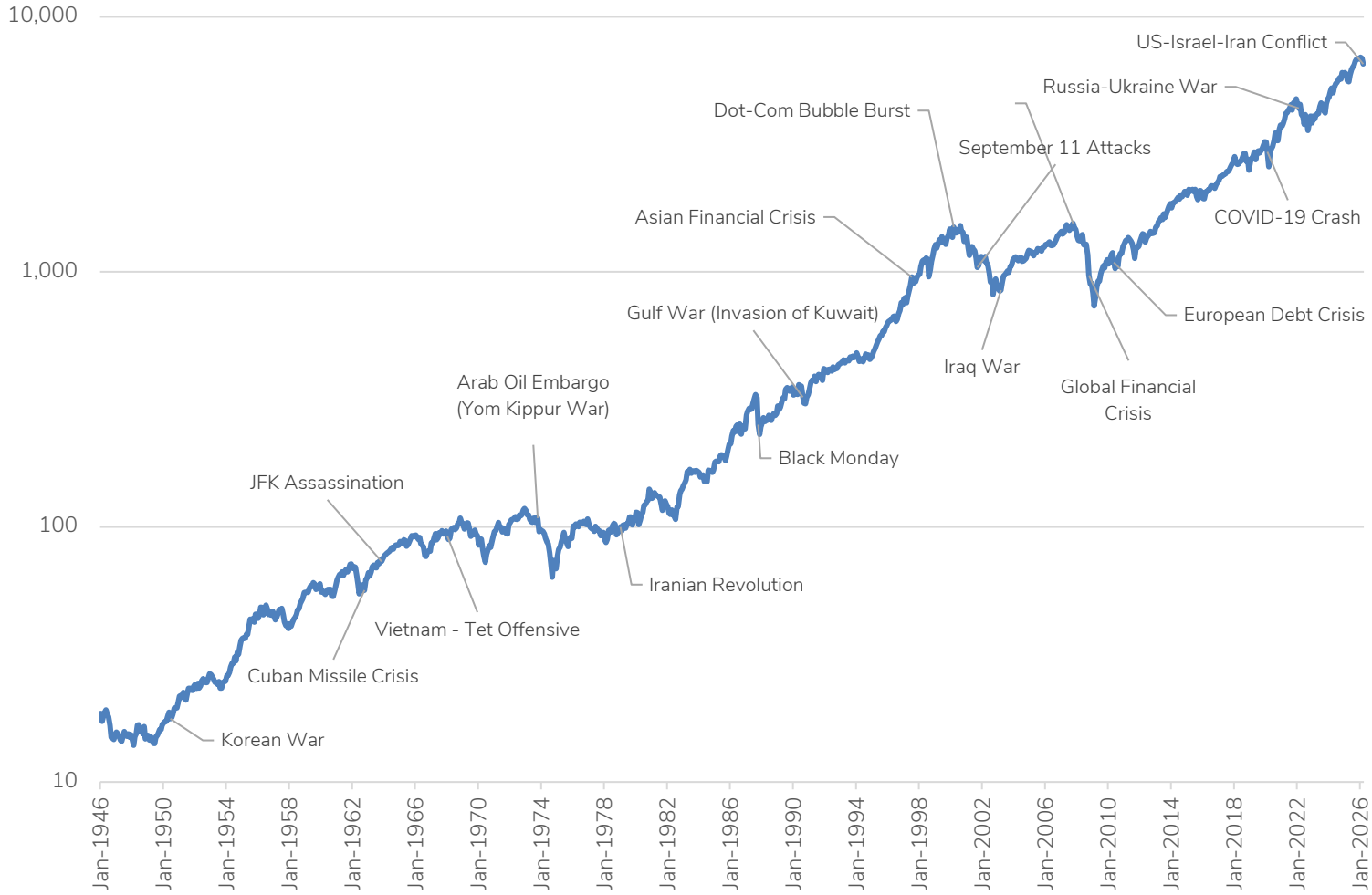
"Bull Markets Climb a Wall of Worry"

As the old saying suggests, there is always a crisis or concern in every bull market rally. Indeed, the last 80 years have seen the S&P 500 Index gain nearly 8% annually (11% with dividends reinvested), despite persistent conflicts, disasters, and economic downturns, as the graph on the next page shows. (Note the calibration of the vertical axis here: The growth is logarithmic!)

While it may seem like "This is it, we should sell!," time and time again, over the long-term the economy has continued to grow, and public companies have continued to grow earnings alongside it. At Mitchell Sinkler & Starr we always try to remind our clients to stay focused on their long-term goals and expect volatility over shorter periods — for without short-term risk, there is no long-term reward.

- Mitchell Sinkler & Starr's Portfolio Managers

S&P 500 Index (excluding dividends)



Source: Bloomberg Finance, L.P.

Economic and Capital Markets Data

	March 31, 2026	(One Year) March 31, 2025	(Three Years) March 31, 2023	(Five Years) March 31, 2021
S&P 500 Index	6529	5612	4109	3973
Price / Earnings Ratio	23.5	24.0	19.7	32.4
Dividend Yield	1.24%	1.39%	1.68%	1.46%
Federal Funds Rate	3.50%	4.25%	4.75%	0.25%
10-Year U.S. Treasury Yield	4.32%	4.21%	3.47%	1.74%
Gold ($ per oz)	4,668	3,086	1,969	1,707
Oil (Brent, $ per barrel)	118	75	80	64
GDP (Annualized)	2.0%	-0.3%	2.6%	4.3%
Unemployment	4.4%	4.2%	3.6%	6.0%
Inflation (Annualized)	2.4%	2.4%	5.0%	1.7%

Federal Funds Rate is Lower Bound

GDP data as of December 31, 2025; Unemployment & Inflation Data as of February 28, 2026;

Sources: U.S. Federal Reserve, Bloomberg Finance L.P., Bureau of Economic Analysis